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Subject

**Call for public input on "Issues included in the annotated agenda of the sixty-fifth meeting of the CDM Executive Board and its annexes"
Annex 15 - Draft Procedure for Addressing Significant Deficiencies**

Honorable Members of the CDM Executive Board,

Thank you for the opportunity to provide input on the Draft Procedure for Addressing Significant Deficiencies. We appreciate that some of the DOE Forum's requests relating to the previous version of the draft procedure have been incorporated, i.e. limiting the liability to negligence and fraud and introducing the date the VVM entered into force as the time limit for the implementation of the procedure. However, the most fundamental concerns of the DOE Forum remain unaddressed. These are specifically:

The need to make risks quantifiable and insurable:

The size of the liability and the degree of risk of being held liable for excess issuance is impossible to quantify under this procedure. The size of the liability itself is a function of the size of the project, and the market price of carbon. Although the a prediction of the number of CERs is made at the validation stage and the length of the crediting period is limited, the market price of carbon fluctuates widely and is impossible to predict over the long term. The degree of risk, on the other hand, is dependent on the possibility of different interpretations of the CDM rules. Furthermore, because there is no precedent or experience of applying this procedure (combined with no limit on liability), it is difficult for insurers to estimate the risk of excess issuance occurring. The difficulty in quantifying the liability and the risk presents a significant uncertainty for insurers. Furthermore, the fact that the procedure does not reference a financial loss by a specific legal entity means that it will not be the result of, or defensible as part of, a normal legal process, which would normally be a pre-requisite under any liability insurance.

The need to segregate the twofold objectives of the draft procedure, namely

- setting of punitive measures in case of fraud and professional negligence, and
- creation of options for the ex-post correction of excess issuance

The current draft provides for liabilities that are in excess of any level required in order to be punitive or to avoid moral hazard. Furthermore, because the liability is not insurable, the procedure would fail to properly correct excess issuance because DOEs are likely to be unable to afford to meet the liabilities, and may go out of business either because they cannot pay, or because they are insolvent as a result of paying.

The need to prevent malpractice by introducing an independent appeals process

We understand that establishing the framework for an independent appeals process for the CDM may be outside the scope of this current procedure; however that is not sufficient grounds to ignore the critical need for such a process before this procedure can be applied. We urge the Board to ensure that a revised procedure for addressing significant deficiencies becomes applicable only once an appeals process is instituted. The lack of any recourse to an independent

body is a fundamental and serious concern under this procedure which has been highlighted in previous DOE Forum submissions.

Feedback from insurers

Following the discussions after EB-64, various DOEs in all regions approached insurance companies to get their views on the recent draft, in particular on the possibility for offering insurance products for the remaining risks. The major concerns which have been expressed by insurers were similar to those raised by the DOE Forum at earlier stages:

- the lack of a definition of professional negligence,
- the inability to quantify the total risk,
- the missing independence of regulatory body and judging body (both by EB) and
- the lack of an independent appeals process.

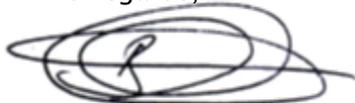
Confronted with this situation insurers clearly expressed that either their products do not cover these risks or that they do not feel able to offer such products at costs which bear any relation to the service costs for validation and verification. Even if the liability is quantifiable or limited, if this limit is too high, the cost of insuring against it would be prohibitive. (Letters of insurance companies will be available for review by EB members at EB-65.)

DOEs neither have the financial background nor access to resources by indirect means (e.g. via insurance as discussed above) to enable them to cover the liability as envisaged in this draft. Introducing the intended liability concept and placing all the burden on DOEs would not deliver the intended integrity of the system, because the DOEs would not be able to meet this burden.

We reiterate our commitment to accept responsibility for causing excess issuance if it results from DOE's professional negligence or fraud. We also accept that punitive measures should be put in place, which can be used in combination with, or instead of, withdrawal of accreditation. However, such a liability will have to be insurable at costs that are reasonable and which would not completely distort the market, and the procedure has to be workable and manageable. Consequently, a re-consideration of this current procedure is vital. As result of the collection of the views of DOEs and their insurance providers, the DOE Forum appeals unequivocally to the EB to desist from the approval of the draft procedure at EB-63, which would damage the whole CDM system without delivering the environmental integrity that the procedure is designed to secure.

We instead suggest organizing a roundtable with members of the CDM Executive Board, members of the UNFCCC Secretariat, representatives of DOEs and representatives of insurers. The expected outcome from this roundtable would be a proposed procedure with the single objective to address cases of fraud and professional negligence that would be insurable at rates that enable all parties to operate the CDM system without a significant increase in costs to the system.

Kind regards,



Werner Betzenbichler
Chair of the DOE/AIE Forum